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Federal Communications Commission
Office of Secretary

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

In the Matter of	)	
McLEODUSA TELECOMMUNICATIONS SERVICES, INC.	)	CC DOCKET NO. 98-84
Petition for Preemption of Nebraska Public Service Commission Decision Permitting Withdrawal of Centrex Plus Service by U S WEST Communications, Inc.	)	

Received

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Common Carrier Bureau
Network Service Division
Office of the Chief

PETITION FOR PREEMPTION, DECLARATORY RULING, AND INJUNCTIVE RELIEF

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Dated: May 29, 1998

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EXECUTIVE SUMMARY

McLeodUSA Telecommunications Services, Inc. ("McLeodUSA"), in an effort to overcome the barriers to the development of local exchange competition created by the Nebraska Public Service Commission's ("PSC") sanctioning of U S WEST's withdrawal of Centrex services, files this Petition for Preemption, Declaratory Ruling, and Injunctive Relief. McLeodUSA is a competitive local exchange carrier ("CLEC") that has used the resale of Centrex services as its primary platform for the delivery of local exchange services to customers in ten states, six of which are in the territory served by U S WEST. Yet, because the Nebraska PSC failed to consider any of the anticompetitive effects of U S WEST's proposed Centrex withdrawal and approved that withdrawal, McLeodUSA is effectively prevented from offering local service in Nebraska. McLeodUSA therefore petitions this Commission to preempt the Nebraska PSC's approval of U S WEST's Centrex withdrawal.

Section 253 of the Communications Act of 1934, as amended by the Telecommunications Act of 1996 (the "1996 Act"), provides the Commission with the authority to preempt any state requirements that may prohibit or have the effect of prohibiting competitive entry into an interstate or intrastate telecommunications market. The Nebraska PSC's sanctioning of U S WEST's Centrex withdrawal has erected a barrier to entry by resellers such as McLeodUSA. Rather than looking at how U S WEST's proposed withdrawal of Centrex (only three days before the 1996 Act became law) might violate the local competition provisions of the 1996 Act, the Nebraska PSC merely sought an express prohibition on service withdrawal in the 1996 Act and this Commission's orders, and finding none, in November 1996 approved the withdrawal as consistent with state and federal law.

In making this decision, the Nebraska PSC overlooked the Commission's admonition to state commissions in its *Local Competition Order* that states should monitor the "anticompetitive effects" of service withdrawals and the requirement that state commissions "ensure that procedural mechanisms exist for processing complaints regarding incumbent LEC withdrawals of services." If the Nebraska PSC had ever turned its attention to sections 251(b)(1) and 251(c)(4) of the 1996 Act, it would have discovered how U S WEST's proposed service withdrawal would effectively prevent McLeodUSA and other large resellers from entering the Nebraska local exchange market. Instead, the Nebraska PSC "rubber-stamped" U S WEST's proposal, thereby giving official approval to the service withdrawal that has kept McLeodUSA from providing the competitive local exchange service in Nebraska that it has provided in every other U S WEST state surrounding Nebraska.

Section 253 provides this Commission with the jurisdiction and the justification to preempt the Nebraska PSC's sanctioning of U S WEST's Centrex withdrawal. Although the Nebraska PSC's decision does not prohibit entry by all means, section 253 is not limited to express and direct prohibitions on entry. As Commission precedent makes clear, any state requirement – whether statute, regulation, order, or even tariff approval – that has the effect of prohibiting carriers from operating "in the same manner in which they operate in other states" is within the scope of section 253. The Nebraska PSC approved this resale restriction despite clear and convincing evidence of the anticompetitive intent and effect of U S WEST's withdrawal of Centrex. Eleven other state commissions rejected this same anticompetitive effort. This Commission should examine the Nebraska PSC's failure to enforce the 1996 Act, and preempt the order approving U S WEST's Centrex withdrawal as a barrier to entry inconsistent with the pro-competitive resale provisions in the statute.

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PETITION FOR PREEMPTION, DECLARATORY RULING, AND INJUNCTIVE RELIEF

Petitioner McLeodUSA Telecommunications Services, Inc. ("McLeodUSA") respectfully submits this Petition for Preemption, Declaratory Ruling, and Injunctive Relief, pursuant to Federal Communications Commission ("Commission") Rules 1.1 and 1.2, 47 C.F.R. §§ 1.1 and 1.2 (1997), and section 253 of the Communications Act of 1934, as amended by the Telecommunications Act of 1996, Pub. L. No. 104-104, § 101(a), 110 Stat. 70, 47 U.S.C. § 253 (1996) (the "1996 Act").[1]

STATEMENT OF INTEREST

McLeodUSA is a competitive local exchange carrier ("CLEC") operating in ten states in the upper Midwest, six of which (Iowa, Minnesota, North Dakota, South Dakota, Wyoming and Colorado) are in the region in which U S WEST Communications, Inc. ("U S WEST") is the dominant incumbent carrier. McLeodUSA's primary platform for delivering local exchange

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[1] All statutory citations herein, unless otherwise indicated, refer to the Communications Act of 1934, as amended by the 1996 Act.

service is by the resale of Centrex service purchased from the Regional Bell Operating Companies, in this case US WEST.

On February 5, 1996, three days before the 1996 Act became law, U S WEST notified the Nebraska Public Service Commission ("PSC") of its intention to officially "grandfather" and withdraw Centrex[2] as a retail service offering in the Nebraska local exchange marketplace. Simultaneously, U S WEST attempted to withdraw Centrex service from all other jurisdictions within its fourteen-state region.

Centrex was chosen by McLeodUSA in 1993 as its preferred platform for the delivery of resold local exchange service in all of its states, and Centrex remains McLeodUSA's primary platform for local service today. Due solely to the withdrawal of Centrex from Nebraska, McLeodUSA does not today offer local service in that state, even though it does so in the surrounding states on all sides of Nebraska that are in U S WEST's region. The Nebraska PSC's determination that U S WEST could withdraw its Centrex service offering from the Nebraska market has therefore frustrated McLeodUSA's efforts to enter that jurisdiction and provide the benefits of local exchange competition to Nebraska consumers.

STATEMENT OF THE FACTS

McLeodUSA is able to provide competitive local exchange services to its customers through Centrex, which makes use of the existing lines and switching equipment of an incumbent carrier such as U S WEST to provide local service to a designated group of lines. These lines are connected to the incumbent carrier's serving central office switch, and are designated by the Centrex software resident in the switch to be part of McLeodUSA's Centrex "common block"

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[2] In Nebraska, and in most of U S WEST's region, the current version of the Centrex product was known as "Centrex Plus."

within that switch. This common block is not a physical piece of equipment, but rather is a software "partition" of the existing central office switch. McLeodUSA, as the Centrex user, receives a certain package of features on lines connected to the common block, and toll calls from users connected to the common block can be routed over dedicated access facilities to reach an interexchange carrier. This functionality is available to all purchasers of Centrex.

Centrex has been available for more than 20 years, and the resale of Centrex promotes entry into local exchange markets by providing a feature-rich service which can be customized by resellers. Because Centrex service has been provided for many years, a limited form of "OSS" is available to Centrex purchasers, which allows certain changes to locations and features to be made by resellers without the manual intervention of U S WEST.

In its filing withdrawing Centrex service from the Nebraska market, U S WEST stated that it would continue to provide such service to existing retail customers until April 29, 2005, (although severe limitations were placed on the number of Centrex lines that could be added, and establishment of new Centrex common blocks was prohibited). Because the establishment of new Centrex common blocks was forbidden, the effect of the "grandfathering" was to make it impossible for new customers to purchase Centrex service. These announcements by U S WEST had the direct effect of preventing the growth of competition by the resale of Centrex, especially from newly emerging and expanding resellers such as McLeodUSA.

McLeodUSA, then known as McLeod Telemanagement, Inc., timely filed a complaint against U S WEST, opposing the withdrawal of Centrex in Nebraska. MCI Communications Corporation ("MCI") and AT&T Communications of the Midwest, Inc. ("AT&T") filed similar complaints. A hearing was held before the Nebraska PSC on May 30, 1996. The undisputed testimony and evidence at the hearing showed that U S WEST continued to provide Centrex service at retail to subscribers who are not resellers or other telecommunications carriers. The complainants argued that under section 251(c)(4)(A) of the 1996 Act, U S WEST must therefore offer Centrex service for resale at wholesale rates. As Anthony J. DiTirro summarized on behalf of MCI:

> Through its grandparenting plan, U S WEST intends to continue to provide its Centrex Plus service at retail to existing subscribers who are not telecommunications carriers . . . . In addition, customers can add a restricted number of new lines to their existing common block resulting in additional sales of Centrex Plus service. Each one of those sales is a provision of service, which under the federal law requires U S WEST to resell the Centrex Plus service.[3]

John Blake, who testified on behalf of AT&T, agreed: "the Federal Act does not exempt any service from the resale requirement. If a service is provided to customers at retail it must be made available for resale."[4] Mr. Blake also pointed out that the curious timing of U S WEST's Centrex withdrawal, commenting:

> The timing of this action is disingenuous. U S WEST was aware of the requirements of the Act and the likelihood that the President would sign the Act into law. The fact that U S WEST's actions occurred just a few days prior to the actual signing of the Act does not protect U S WEST from the Act's requirements. The resale obligations of Section 251(c)(4) provide a means for new telecommunications competitors to enter the market through the resale of an incumbent telephone company's services at prices that are derived form [*sic*; read: "from"] the incumbent's existing retail rates. U S WEST's proposal is an attempt to stave off such competitive entry in Nebraska to the detriment of local customers and, of course, to U S WEST's potential competitors.[5]

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[3] Tr. at 37, and Hearing Exhibit 3.

[4] Tr. at 73-74, and Hearing Exhibit 4.

[5] Tr. at 74, and Hearing Exhibit 4.

On behalf of McLeod Telemanagement, Thomas Parvin similarly testified: "U S WEST made its announcement on February 5, 1996, in an attempt to avoid the application of the Telecommunications Act of 1996 signed by President Clinton on February 8, 1996."[6]

Despite this testimony and evidence, the Nebraska PSC failed to consider the anticompetitive effects of the withdrawal under federal law. There was extensive testimony about this issue at the PSC's hearing on May 30, 1996. U S WEST argued, however, that the Nebraska PSC had no jurisdiction to review the withdrawal under the 1996 Act:

> Since no interconnection agreement or rural exemption is involved in this case, the Commission has no authority to decide whether U S WEST's withdrawal and grandfathering of Centrex Plus service is in violation of the Federal Act.[7]

When the PSC issued its Order on the matter six months later on November 25, 1996 (a copy of which is provided as Exhibit A with this Petition), there was no discussion of potential anticompetitive effects at all, nor was there any analysis of whether the withdrawal would circumvent or undermine the goals embodied in federal law. Instead, the majority of the Nebraska PSC simply ignored the anticompetitive effects of the withdrawal. The Nebraska PSC relied upon Nebraska state law, and found that there was no prohibition against U S WEST's actions there. Next, citing federal law and the 1996 Act, the Nebraska PSC stated that in "adopting the Telecommunications Act of 1996, Congress delegated general enforcement powers to the Federal Communications Commission (FCC)." The Nebraska PSC finally concluded that U S WEST's withdrawal of Centrex had to be, or at least was to be, approved because the "FCC declined to adopt a rule on the subject of the ability of an incumbent local exchange carrier to

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6 Tr. at 15, and Hearing Exhibit 2.

7 U S WEST Brief, at 20.

withdraw services" and because the FCC had left the matter for state commissions to resolve.[8] The PSC did not believe itself required to, and did not, examine whether the anticompetitive effects of the withdrawal violated sections 251(c)(4) or 251(b)(1) of the 1996 Act.[9]

ARGUMENT

I. THE NEBRASKA PSC'S SANCTIONING OF U S WEST'S WITHDRAWAL OF CENTREX HAS THE EFFECT OF PROHIBITING COMPETITIVE ENTRY.

Section 253(a) of the 1996 Act prohibits state requirements that "may prohibit or have the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service."[10] The Nebraska PSC's sanctioning of U S WEST's Centrex withdrawal in the *Nebraska Order*, which is based upon a failure to substantively consider the competitive implications of this withdrawal under federal law, has had the clear effect of prohibiting competitive entry by McLeodUSA and unreasonably restricting the means by which all CLECs enter and provide service in the Nebraska market. The Commission should act pursuant to section 253 to preempt the anticompetitive barrier to entry erected by the Nebraska PSC, so that competitors such as McLeodUSA are able to enter the Nebraska local exchange market as envisioned by the 1996 Act, free from onerous restrictions intended by U S WEST to inhibit competitive entry.

A. Section 253 Prohibits State Actions That Have the Effect of Prohibiting Competitive Entry.

Section 253(d) provides this Commission with the jurisdiction to preempt the enforcement of any statute, regulation, or legal requirement imposed by a state that violates

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[8] Nebraska PSC Opinions and Findings, at 5 (Nov. 25, 1996) ("*Nebraska Order*").

[9] 47 U.S.C. §§ 251(c)(4) and (b)(1) (1996).

[10] *Id.* at § 253(a).

subsections (a) or (b) of section 253. As noted above, section 253(a) does not merely address state actions that actually "prohibit" competitive entry – statutes, rules, or orders that prevent any CLEC from providing service in the market. This statute also recognizes that the state action may be more subtle, foreclosing only certain methods of entry or enforcing requirements that effectively permit only the incumbent to provide service in the market. Thus, even though a state action may not rise to the level of an express prohibition on competitive entry, this Commission has the authority to preempt any state action that increases the costs of competitive entry or unreasonably limits the methods by which a CLEC may enter the market.[11] As this Commission concluded in the *Texas Preemption Order*, section 253 "requires us to preempt not only express restrictions on entry, but also restrictions that indirectly produce that result."[12]

A state commission's official sanctioning by Order of an incumbent's anticompetitive actions can (and in this case, does) have the same effect of prohibiting competitive entry as any affirmative barrier to entry raised at the initiative of a state legislature or commission by statute, regulation, or order.[13] The precise question for this Commission to consider is whether the Centrex withdrawal approved by the Nebraska PSC "materially inhibits the ability of any

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[11] *See Petitions for Declaratory Ruling and/or Preemption of Certain Provisions of the Texas Public Utility Regulatory Act of 1995*, CCB Pol 96-13, 96-14, 96-16, 96-19, Memorandum Opinion and Order, 13 FCC Rcd 3460, 3497 (1997) ("*Texas Preemption Order*"), at ¶ 75 (finding that "it is reasonable to read section 253(a) in conjunction with the definition of telecommunications service as barring restrictions by states or localities on the means through which an entity may enter the local exchange market").

[12] *Texas Preemption Order*, 13 FCC Rcd at 3480, ¶ 41.

[13] *See also Texas Preemption Order*, 12 FCC Rcd at 3563, ¶ 222 (preempting "a case in which the Texas Commission has upheld the enforcement of a resale restriction in SWBT's centrex resale tariff").

competitor or potential competitor to compete in a fair and balanced legal and regulatory environment."[14]

B. This Commission Should Consider the Anticompetitive Implications of the Nebraska PSC's Order.

Although the Nebraska PSC held a hearing on the legality of U S WEST's Centrex withdrawal, the PSC failed to engage in any substantive scrutiny of U S WEST's actions pursuant to the local competition provisions of the 1996 Act. Instead, the PSC looked first to state law, and finding no restriction on withdrawal there, looked directly to this Commission's *Local Competition Order* for express guidance on when service withdrawal may be permissible.[15] Cursorily reviewing the *Local Competition Order*, the PSC correctly stated that "the FCC declined to adopt a rule on the subject of the ability of an incumbent local exchange carrier to withdraw services" where resellers are purchasing such services for resale in competition with the incumbent, because this Commission found "that this is a matter best left to state commissions."[16] The Nebraska PSC then issued its decision approving the withdrawal of Centrex service without ever looking to the provisions in the 1996 Act that actually govern the restrictions that incumbents may place upon competitive resale of their services.

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[14] *California Payphone Association Petition for Preemption of Ordinance No. 576 NS of the City of Huntington Park, California Pursuant to Section 253(d) of the Communications Act of 1934*, CCBPol 96-26, Memorandum Opinion and Order, 12 FCC Rcd 14191, 14206 (1997) ("*Huntington Park Order*"), at ¶ 31.

[15] *See Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98, First Report and Order, 11 FCC Rcd 15499 (1996) ("*Local Competition Order*").

[16] *Nebraska Order*, at 5. *See also Local Competition Order*, 11 FCC Rcd at 15978, ¶ 968.

The PSC's selective reading of the *Local Competition Order* caused it to overlook an important provision in that Order that required it to consider all of the competitive implications of Centrex withdrawal. Just because this subject matter was left for state commissions to decide does not mean that state commissions are free to ignore the provisions of the 1996 Act in considering how withdrawal affects the development of a competitive marketplace. This Commission could not have been more clear when it expressed concern about the "anticompetitive effects" of service withdrawals and directed state commissions to "ensure that procedural mechanisms exist for processing complaints regarding incumbent LEC withdrawals of services."[17] The Nebraska PSC was obligated under federal law to engage in a thorough and thoughtful analysis (such as that recommended by PSC Commissioner Johnson in dissent) in considering the anticompetitive implications of U S WEST's Centrex withdrawal.[18] The PSC's failure to consider whether U S WEST's actions violated the 1996 Act by impermissibly limiting the methods of competitive entry highlights the need for this Commission to itself engage in a substantive examination of the patently discriminatory effects of the PSC's decision.

Indeed, the only reasonable reading of the *Local Competition Order*, and the Commission's findings regarding the withdrawal of services, requires that state commissions examine a withdrawal of service to determine whether that withdrawal will act as a barrier to entry or unreasonably restrict the resale of services. It is only *after* such a determination is made that withdrawal or "grandfathering" can be allowed. The Nebraska PSC's failure to engage in this kind of a substantive examination, and its resulting approval of U S WEST's unreasonable and discriminatory resale restriction, should prompt this Commission to preempt the Nebraksa

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17 *Local Competition Order*, 11 FCC Rcd at 15978, ¶ 968.

18 *See Nebraska Order*, at 7-8.

PSC's decision as inconsistent with the pro-competitive provisions and procedures required by federal law.

C. Centrex is Essential to the Provision of Local Exchange Service by McLeodUSA and Other Resellers in Nebraska, and the Withdrawal of Centrex Discriminates Against Competitors in Violation of Section 251(b)(1) and Section 251(c)(4).

The withdrawal of Centrex proposed by U S WEST and approved by the PSC forecloses entirely a method of entry that large resellers such as McLeodUSA have relied upon to enter other markets throughout the U S WEST region.[19] While one would think carriers generally withdraw services only when there is no demand for the service, or the service is replaced with a better, less expensive substitute, Centrex is in demand by both competitors and consumers nationwide.[20] Centrex is more attractive and useful to competitors than resale of PBX services, because Centrex equipment is located at a central office, and gives the reseller access to all customers served by the central office. Furthermore, Centrex allows carriers to add or remove vertical features offered to customers on a relatively simple basis, thereby enhancing the service they can promise to consumers.

U S WEST's withdrawal of Centrex is inconsistent with the normal practice in the industry. This was explained to the Nebraska PSC by McLeod witness Thomas Parvin:

> In my experience in the telecommunications industry, withdrawing an existing service before a replacement service is offered is a very questionable step. Typically, a replacement offering would be made available, and customers would migrate to that offering;

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[19] As noted below, eleven other states in U S WEST's region have already ruled that U S WEST efforts to withdraw Centrex service are anticompetitive and in violation of state or federal law.

[20] Evidence for this proposition can be found in the fact that U S WEST's attempt to withdraw Centrex throughout its region has been vehemently opposed by competitors, who presumably would not be interested in the service unless it were attractive as a means of serving retail customers.

> then, when use of the older offering had dwindled, it would be declared "obsolete." The obsolete offering is typically replaced with a "better" offering: something with better service characteristics, more features, lower price, better customer service, etc. I cannot recall another case where an important product was withdrawn before a replacement was available. This is especially true where a substantial, and as far as McLeod is concerned, growing demand for the service still exists. A firm operating in a competitive market would not serious [*sic*: seriously] consider withdrawing a product still in demand by customers without first offering a superior substitute.[21]

Any doubt about the unusual nature of U S WEST's action was dispelled by its own witness, who testified under cross-examination at hearing that never before had U S WEST's "grandfathering" actions in Nebraska left *no* Centrex product at all available to new customers in the state.[22]

In fact, Centrex provides an economically efficient means of entering the local exchange market because resellers can break down the bulk product they purchase from incumbents to provide service to smaller customers. Entry by such means is fully consistent with the Commission's directives regarding the development of local competition. The Commission has "generally not allowed carriers to prevent other carriers from purchasing high-volume, low price

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21 Tr. at 11, and Hearing Exhibit 2.

22 Tr. at 129. At the time of the withdrawal filing in Nebraska (and elsewhere), U S WEST did promise that a "replacement" product would be available by the fall of 1996. In fact, the Nebraska PSC relied at least in part upon testimony containing such a promise in approving U S WEST's actions. *See Nebraska Order*, at 3. Once again, however, U S WEST's actual conduct is telling. U S WEST has introduced a "small user" version of Centrex (called "Centrex 21") in most of its states. This version of the product is designed for smaller users; it is not generally attractive to resellers such as McLeodUSA, and in fact is used to directly compete for the same customers to which McLeodUSA would typically market its services. U S WEST has yet to generally introduce the "large user" version of the product that would be appropriate for resellers. In those few states where this product (called "Centrex Prime") has been introduced, U S WEST's actions again leave no doubt as to its motivation: Centrex Prime has no set tariff pricing which would allow it to be purchased by resellers at a wholesale discount, and as discussed below, it contains an overt restriction on traffic aggregation which achieves exactly the same result held unlawful by the Commission in the *Texas Preemption Order*. *See* Section I.E., *infra*.

offerings to resell to a broad pool of lower volume customers."[23] Yet this is exactly the type of "arbitrage" that U S WEST apparently believes must be prevented through the withdrawal of Centrex in Nebraska.[24] Furthermore, the Commission found restrictions on the resale and trunking of flat-rated services to multiple customers to be presumptively unreasonable, noting that "[w]e do not believe that these or other efficient uses of technology should be discouraged through restrictions on the resale of flat-rated offerings to multiple end users, even if incumbent LECs have not always priced such offerings assuming these usage patterns."[25] Finally, the Commission held that LECs could not require the individual end user customers of resellers to each meet requirements for a volume-discount; but rather the usage of all the reseller's customers could be aggregated in order to reach the discount amount.[26]

Contrary to these principles, allowing the withdrawal of Centrex effectively forecloses an efficient and essential means of entry that carriers such as McLeodUSA utilize to enter local exchange markets. In the 1996 Act, Congress gave competitors three options for entering the nation's local exchange markets: (1) building their own network and interconnecting with the incumbent; (2) purchasing the unbundled network elements of the incumbent and combining them with the competitor's own network elements; or (3) reselling the telecommunications services of the incumbent.[27] In its rulings on section 271 applications, this Commission has

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[23] *Local Competition Order*, 11 FCC Rcd at 15974, ¶ 958.

[24] *See* II.C., *infra*.

[25] *Local Competition Order*, 11 FCC Rcd at 15975-76, ¶ 963.

[26] *Local Competition Order*, 11 FCC Rcd at 15971, ¶ 953.

[27] 47 U.S.C. §§ 251(c)(2), (3), & (4) (1996).

made clear that it considers the resale entry strategy to be as important as interconnection and use of unbundled network elements:

> It is essential for local competition that the various methods of entry into the local telecommunications market contemplated by the Act – construction of new facilities, purchase of unbundled network elements, and resale -- be truly available.[28]

Similarly, in the *Texas Preemption Order*, this Commission noted that not all methods of entry need to be foreclosed in order for a state action to constitute a barrier to entry. Specifically, the Commission found that a state may not "require that an entity provide telecommunications services via its own facilities and limit the entity's ability to resell incumbent LEC services or restrict the use of unbundled network elements provided by the incumbent."[29]

The Commission's insistence upon the availability of resale options is grounded in the 1996 Act. Section 251(b)(1) states that each local exchange carriers is "not to prohibit, and not to impose unreasonable or discriminatory conditions or limitations on, the resale of its telecommunications services."[30] Similarly, section 251(c)(4) imposes upon U S WEST and other incumbent local exchange carriers the duty "not to prohibit, and not to impose unreasonable or discriminatory conditions or limitations on, the resale of such telecommunications service . . . ."[31] U S WEST's attempted withdrawal of Centrex service only three days before these provisions became law was an obvious effort to circumvent the duties imposed by these provisions.

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[28] *In the Matter of Application of Ameritech Michigan Pursuant to Section 271 of the Communications Act of 1934, as Amended, to Provide In-Region, InterLATA Services in Michigan*, CC Docket No. 97-137, Order (1997), at ¶ 21.

[29] *Texas Preemption Order*, 13 FCC Rcd at 3496, ¶ 74.

[30] 47 U.S.C. § 251(b)(1) (1996).

[31] *Id.* at § 251(c)(4).

Yet, rather than considering U S WEST's anticompetitive actions in light of these important sections of the 1996 Act, the Nebraska PSC simply "rubber stamped" U S WEST's proposal after it could find no express prohibition on withdrawal under Nebraska law or in the *Local Competition Order*. By contrast, numerous other state commissions have satisfied their obligation to review and enforce sections 251(b)(1) and 251(c)(4), and rejected outright identical attempts by U S WEST to withdraw Centrex as violative of federal law. For example, the South Dakota Public Utilities Commission ruled that U S WEST's withdrawal of Centrex-like services in that jurisdiction was a violation of its resale obligations under section 251(c)(4)(B) of the 1996 Act and "an attempt to avoid" the 1996 Act's resale requirements, as well as being discriminatory under state law.[32] Similarly, the Wyoming Public Service Commission rejected an identical effort by U S WEST, concluding that "approval of the Centrex Plus filing is not in the public interest and will hinder and delay the opening of the local exchange market to competition within the state of Wyoming."[33] Specifically, the Wyoming Commission noted that U S WEST's proposed withdrawal "violates certain provisions of the Federal Act, to-wit: Sections 251(b)(1) and 251(c)(4) . . . ."[34]

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32 *In the Matter of the Application of U S WEST Communications, Inc. to Discontinue its Centrex Plus Services to New Customers*, Docket No, T96-023, Final Order (S.D.P.U.C. Aug. 22, 1996) ("*South Dakota Order*"), at 3-4.

33 *In the Matter of the Tariff Filing of U S WEST Communications, Inc.*, PSC Docket No. 70000-TT-96-279, Memorandum Opinion, Findings, and Order (Wy. P.S.C. Sept. 6, 1996), at 23.

34 *Id.*, at 24.

Unlike these other commissions, the Nebraska PSC never considered the competitive ramifications of U S WEST's discriminatory actions under federal law.[35] As a result of the superficial examination made by the Nebraska PSC without reference to the federal statutory prohibitions against resale restrictions and barriers to entry, resale of U S WEST's Centrex services is not available in Nebraska today. The PSC-sanctioned absence of Centrex "materially inhibits the ability" of McLeodUSA "to compete in a fair and balanced legal and regulatory environment,"[36] as McLeodUSA has not been able to enter the Nebraska market in the same manner as it has in every other state. The Nebraska PSC's approval of the unreasonable and discriminatory Centrex withdrawal in its *Nebraska Order* should therefore be viewed as a barrier to entry that has the effect of inhibiting competitive operations by McLeodUSA and other carriers in U S WEST's Nebraska service territory.

D. The Nebraska PSC's Order Permitting Centrex Withdrawal Should be Preempted Under Section 253 Because the Order Sanctions the Anticompetitive Effects of Centrex Withdrawal.

Because entry into the Nebraska local exchange market by McLeodUSA has been materially inhibited by U S WEST's withdrawal of Centrex, the Nebraska PSC's official sanction of this patently anticompetitive action in its *Nebraska Order* constitutes a barrier to entry in violation of section 253(a). Under section 253(d), this violation provides the

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[35] The Nebraska PSC's only consideration of the discrimination claims raised by complainants was under state case law, and it can be summarized as follows: "[I]n the area of utility service, it is not every discrimination by a telephone company or other utility that is objectionable but only such discriminations that are *unjust or arbitrary*." *Nebraska Order*, at 4 (emphasis added). This, of course, is not the standard set forth in section 251 — unreasonable *or* discriminatory conditions alone are sufficient, whether or not they are also "unjust" or "arbitrary." Thus, even if the PSC believed that U S WEST's proposal did not constitute discrimination under state law, it still had an obligation to consider whether U S WEST's conduct violates the different pro-competitive standards of the 1996 Act as well.

[36] *See Huntington Park Order*, 12 FCC Rcd at 14191, ¶ 31.

Commission with the authority and justification to preempt the Nebraska PSC's decision, so that Centrex service may be made available for resale on reasonable and nondiscriminatory terms.

McLeodUSA recognizes that the Nebraska PSC's decision may in effect be "saved" by the preservation of state authority set forth in section 253(b) if it meets certain criteria. As this Commission stated in its *Silver Star Telephone Order*, even if state actions are proscribed by section 253(a), "we then determine whether they fall within the exception to section 253(a)'s proscription set forth in section 253(b). . . . If the [state actions] satisfy section 253(b), they are not preemptable under section 253(d), even if they are inconsistent with section 253(a), considered in isolation."[37]

The Nebraska PSC's decision is not saved by the preservation of state authority set forth in section 253(b). This subsection provides specific exceptions to subsection (a), stating that nothing in section 253 "shall affect the ability of a State to impose, on a competitively neutral basis . . . requirements necessary to preserve and advance universal service, protect the public safety and welfare, ensure the continued quality of telecommunications services, and safeguard the rights of consumers." None of these issues appears to have been considered by the Nebraska PSC in approving the withdrawal, and in fact, allowing U S WEST to withdraw Centrex from the Nebraska local exchange market fits none of these categories — it has no relation to universal service, does not protect public safety or welfare, does not ensure the continued quality of telecommunications services, and was not intended to safeguard the rights of consumers. (Indeed, if the Centrex withdrawal truly involved a matter of public safety and welfare, quality of service, or consumer rights, presumably U S WEST would have needed to withdraw the service

[37] *Silver Star Telephone Company, Inc. Petition for Preemption and Declaratory Ruling*, CCBPol 97-1, Memorandum Opinion and Order, 12 FCC Rcd 15639, 15656 (1997), at ¶ 37.

entirely because of such problems, rather than simply grandfathering the service for existing customers.)

Moreover, the restriction is hardly competitively neutral, as it forecloses entirely an essential and efficient method of entry that large resellers such as McLeodUSA have relied upon to enter other markets throughout the U S WEST region.[38] As noted above, McLeodUSA believes that resale of U S WEST's telecommunications services is not "truly available" in Nebraska as a result of the Nebraska PSC's decision. Carriers such as McLeodUSA who have successfully used Centrex resale to enter other local exchange markets are effectively precluded from providing service in Nebraska, simply because U S WEST's eleventh-hour withdrawal of Centrex was sanctioned by the PSC without any substantive examination. Thus, the sanctioning of Centrex withdrawal in the *Nebraska Order* should be preempted because it constitutes a barrier to entry that has had the effect of inhibiting competitive operations by McLeodUSA and other carriers in U S WEST's Nebraska service territory.

E. The Commission's *Texas Preemption Order* Compels Preemption of the Nebraska PSC's Approval of the Withdrawal of Centrex Plus.

The Commission should act in accordance with its own precedent to preempt the Nebraska PSC's order permitting U S WEST to withdraw Centrex service. Southwestern Bell Telephone Company's tariffs included a "continuous property restriction" ("CPR") that limited a Centrex reseller's ability to use resold Centrex service to offer competitive local service to unrelated customers in diverse locations, the adoption of which had been approved by the Texas Public Utilities Commission in 1994. In its *Texas Preemption Order*, the Commission concluded

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[38] Eleven other states in U S WEST's region have already ruled that U S WEST's efforts to withdraw Centrex service are anticompetitive and in violation of federal or state law. *See* Section II.B, *infra.*

that the CPR was an unreasonable restriction on Centrex Plus resale in violation of section 251(c)(4)(B) of the Telecommunications Act of 1996, and that enforcement of the provision by the Texas Public Utilities Commission violated section 253(a) of the Act.[39] Specifically, the Commission found that preventing a competitive provider from operating "in the same manner in which they operate in other states" due to a resale restriction "has the effect" of prohibiting the ability of the "entity to provide a telecommunications service, *i.e.*, centrex service, through resale in violation of the provisions of section 253(a) of the Act."[40] Although SWBT has applied for reconsideration, the *Texas Preemption Order* remains in effect and constitutes existing Commission precedent on the reasonableness of Centrex resale restrictions.

Simply stated, withdrawal of Centrex is the ultimate resale "restriction." U S WEST admitted in various proceedings that the withdrawal and grandfathering of Centrex service throughout its region were intended to prevent resale of Centrex service. Logic dictates that if merely restricting aggregated resale of Centrex service is an unreasonable restriction on resale, then sanctioning the complete withdrawal of Centrex service to avoid the resale obligation altogether is an unreasonable restriction on resale that violates the federal act and must be preempted.

When the Nebraska PSC approved U S WEST's proposed withdrawal of Centrex Plus service, the *Nebraska Order* unequivocally prevented (and continues to prevent) McLeodUSA from operating "in the same manner in which [it] operates in other states." U S WEST knew that McLeodUSA used resold Centrex service to offer competitive local service, and that withdrawal

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[39] *Texas Preemption Order*, 13 FCC Rcd at 3561-67, ¶¶ 218-226, 230.

[40] *Texas Preemption Order*, 13 FCC Rcd at 3561-62, ¶ 220.

of Centrex would prevent McLeodUSA from offering competitive local service in Nebraska.[41] The Nebraska PSC's official sanction of U S WEST's anticompetitive action constitutes an unreasonable restriction on resale and has created an insurmountable barrier to McLeodUSA's entry into Nebraska in violation of 47 U.S.C §§ 253(a) and 251(c)(4)(B).

II. THERE IS CLEAR AND CONVINCING EVIDENCE OF THE ANTICOMPETITIVE INTENT AND EFFECT OF U S WEST'S WITHDRAWAL OF CENTREX.

By proposing to withdraw Centrex service only three days before the 1996 Act became law, U S WEST clearly intended to limit the availability of this service to competitors who would soon seek to enter the Nebraska local exchange market. In fact, there are four separate sets of evidence that clearly prove that, had the Nebraska PSC conducted a thorough and searching analysis of U S WEST's withdrawal of Centrex service as required by the 1996 Act and directed by the *Local Competition Order*, it would have found the withdrawal anticompetitive and in violation of several provisions of the 1996 Act. Thus, in reviewing the effect of the Nebraska PSC's decision, the Commission should also consider the following items:

A. The dissent, on the same record and in a substantive analysis, clearly found the withdrawal anticompetitive and in violation of the 1996 Act;

B. The state commissions in Oregon, Iowa, South Dakota, North Dakota, Colorado, Utah, Minnesota, Wyoming, Washington, Arizona, and New Mexico have all found the exact same withdrawal of Centrex by U S WEST to be anticompetitive and in violation of federal law;

C. U S WEST's own executives stated that the purpose of the withdrawal was to avoid "arbitrage" – a euphemism for competition by resale;

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[41] In fact, less than two weeks before U S WEST withdrew and grandfathered Centrex service, senior management from McLeodUSA met with senior representatives of U S WEST and informed U S West of McLeodUSA's plans to quickly expand its operating area to include several additional states in U S WEST's region, including Nebraska, via resold Centrex Plus service. U S WEST knew that its withdrawal of Centrex service would completely thwart McLeodUSA's plans to enter Nebraska markets.

D. No functionally equivalent service for large resellers capable of allowing meaningful resale was offered then or since.

A. The Nebraska PSC Dissent, On The Same Record And In A Substantive Analysis, Clearly Found The Withdrawal Anticompetitive And In Violation Of The 1996 Act.

One Nebraska PSC commissioner, Commissioner Lowell C. Johnson, did conduct an in-depth analysis of the record in this case, and the anticompetitive effects of the withdrawal, and found a compound violation of the 1996 Act therein. Commissioner Johnson's entire discussion of how the 1996 Act governs in this area is quoted below for this Commission's review, and to offer a clear contrast to the simplified analysis provided by the Nebraska PSC majority:

> The majority's adoption of the procedure required by the FCC at paragraph 968 of its First Report and Order, allowing resale only to the "grandfathered customers of U S WEST," orders U S WEST to do nothing more than comply with an existing legal obligation. *The majority relies upon this provision to avoid examining the substantive requirements of the Telecommunications Act of 1996 ("Act") itself.*
>
> The Act creates a pro-competitive framework designed to bring competition to local exchange markets. The Act specifically (i) prohibits unreasonable or discriminatory restrictions on resale [47 U.S.C. §251(b)(1)], (ii) requires wholesale rates for all services offered at retail [47 U.S.C. §251(c)(4)(A)], and (iii) forbids the erections of barriers to entry into exchange markets [47 U.S.C. §253]. *The evidence before the Commission showed that U S WEST's filing will have the effect of imposing a barrier to the entry of competitors into local exchange markets, in clear violation of 47 U.S.C. §§ 251 (b)(1) and 253.* Furthermore, the withdrawal of Centrex Plus service as proposed by U S WEST will effectively circumvent the "resale" requirement of the Act, because U S WEST has not offered either a more feature rich competitive product or a functionally equivalent replacement. U S WEST's withdrawal of Centrex Plus, under such circumstances, thus *violates 47 U.S.C. §251(c)(4)(a) as well.* Finally, allowing some customers to expand Centrex Plus service, while denying the same Centrex Plus service to other interested customers, is testimony to the fact that Centrex Plus is not truly withdrawn, and serves to emphasize that U S WEST's proposal to "withdraw" or